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SUBJECT: GOP AT ODDS WITH PETROLEUM INDUSTRY

This cable is the first in a two part series on the Energy Sector in Panama

1.SUMMARY (SBU) The sharp increase in global oil prices prompted demonstrations and transportation strikes during September and October. In a country where 40% of the population already live in poverty, the price of a basic commodity has more than doubled this year. The GOP responded by abruptly changing existing fuel price regulations and giving itself a legal avenue to potentially assume control of privately owned storage facilities. The GOP also exempted the transport sector from diesel fuel tax, losing revenue at a time of budget deficit. The petroleum industry maintains these short term solutions have caused them economic harm, jeopardized the investment climate, and damaged the relationship between the industry and the GOP. In the absence of a cohesive energy plan designed to reduce dependence on foreign oil, the GOP is scrambling to deflect responsibility and appear proactive through the hasty announcement of energy development projects of undetermined viability, benefit or length. No plans to participate in Venezuela's Petrocaribe have been announced. END SUMMARY.

GOP CHANGES OIL PRICE RULES

12. (U) Panama imports 100 percent of its fossil fuel and despite excellent use of hydro electricity, almost half of Panama's energy consumption depends on oil. Three global petroleum companies currently service the Panamanian market, Chevron-Texaco, Exxon-Mobil and Shell-BP. Exxon-Mobil and Chevron-Texaco representatives told Emboffs that regulatory and market reforms in Panama from 1992 to 2002 successfully created a highly competitive market and some of the lowest prices in Central America.

13. (SBU) Since September 2003, the rack price of imported fuel in Panama has been published every 14 days by the GOP using international costs of supply, transport and storage. In September 2005, the GOP began lowering the effective period to 7 days whenever global oil prices fell and held to the 14 days whenever global oil prices rose, making it impossible for an importer to calculate costs or project revenue. Exxon-Mobil President of the Inter-Americas, Jesse Owens told Emboffs he did not expect to profit on every shipment to Panama, but that the actions undertaken by the GOP had made the market unprofitable for the foreseeable future.

14. (SBU) In April 2005 the GOP changed existing regulations to allow the occupation and utilization of the country's only fuel storage infrastructure (currently owned and operated by Chevron-Texaco) "for any situation which might affect the supply of refined products." Chevron-Texaco country manager believes this undermines the integrity of their substantial in-country fuel storage assets.

15. (SBU) The GOP has also foregone diesel fuel tax revenue to reduce prices for the transport industry, through a designated list of retail outlets who may sell diesel tax free. Industry representatives maintain that this list of distributors does not correspond to the purchasing patterns of the transport industry and the allocated volumes far exceed those used by the transport industry. In conjunction with the American Chamber of Commerce, the industry has protested their forced compliance with this program, asserting it could result in a black market in diesel.

16. (U) An Amcham board member and retired oil executive told Econoff that the GOP's politically expedient attempts to shelter the populace and the economy from the impact of rising global oil prices were potentially more destabilizing than the prices themselves because they threatened the stability of the supply and reduced revenue at a time of deficit hindering the GOP's ability to invest in alternate fuels.

GOP RESPONSE TO INDUSTRY CONCERNS

17. (SBU) Vice-Minister of Industry Manuel Paredes told Emboffs the GOP feels squeezed between domestic constituencies expecting to be shielded from the global rise in fuel prices and the fuel companies expecting to make a profit. Paredes questioned the financial damages claimed by the petroleum companies, suggesting they write off their losses against their global profits. However, he conceded the GOP had erred by destabilizing existing regulation. Emboffs emphasized the importance of a stable investment climate to Panama's development strategy. Paredes said the GOP is structurally incapable of administering a secure and transparent diesel fuel subsidy program for the transport sector such as checks, ATM cards, or coupons directly to the transport fuel purchasers.

18. (SBU) In August 2005, the GOP announced its first policy on hydrocarbons and alternate energy sources. This "policy" is a hastily cobbled together set of desired infrastructure and capacity with minor efforts at conservation. (To conserve energy, new government working hours are 7:30 am to 3:30 pm.) To diversify its energy sources, the GOP proposes recouping its refining capacity through a joint venture with Mexico, a natural gas pipeline with Columbia, and the development of alternate fuel sources such as wind, solar and peat. However, neither the financial viability nor the projected length of any project has been established.

19. (SBU) Comment: As Panama is not in a position to meaningfully affect the global price of oil, avoiding further degradation of living standards requires the GOP to tackle the long-term challenges of high unemployment, disparate income distribution, corruption, and completing Social Security and Judicial reforms. Industry representatives told Emboffs that the rack price and effective period had stabilized at an acceptable level but made it clear they did not want to subsidize GOP short term political solutions again. End Comment.
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